Lornex

MINING CORPORATION LTD.

ANNUAL REPORT 1973

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OFFICERS	Honorary Chairman - - - - - - - - E. H. LORNTZSEN Chairman of the Board - - - - - - R. W. WRIGHT, CBE President and Chief Executive Officer - - - R. D. ARMSTRONG Vice-President - - - - - - - - - - G. R. ALBINO Vice-President, General Manager - - - - - C. W. RENO Treasurer - - - - - - - - - - - - J. VAN NETTEN Secretary - - - - - - - - - - - - C. W. M. BURGE
DIRECTORS	G. R. ALBINO, Port Credit, Ont. W. A. ARBUCKLE, Montreal R. D. ARMSTRONG, Toronto E. B. GILLANDERS, Vancouver F. GREGORY, London, England R. HAMMOND-CHAMBERS, Edinburgh, Scotland N. B. IVORY, Montreal K. KAWAKAMI, Tokyo, Japan E. H. LORNTZSEN, Vancouver A. F. LOWELL, Toronto C. W. RENO, Logan Lake, B.C. J. A. SADLER, Toronto R. W. WRIGHT, CBE, London, England
HEAD OFFICE	580 Granville St. - - - - - - - - - - - Vancouver
MINE OFFICE	P.O. Box 1500 - - - - - - - - - - - - Logan Lake
PRINCIPAL BANKERS	Canadian Imperial Bank of Commerce - - Vancouver and Toronto The Toronto-Dominion Bank - - - - - - - - Toronto Bank of Montreal - - - - - - - - - - - Toronto
SOLICITORS	Clark, Wilson & Company - - - - - - - - Vancouver Fasken & Calvin - - - - - - - - - - - Toronto
AUDITORS	Coopers & Lybrand - - - - - - - - - Vancouver
REGISTRAR AND TRANSFER AGENT	National Trust Company, Limited - - - - - - Vancouver
SHARES LISTED	Vancouver Stock Exchange
THE ANNUAL GENERAL MEETING	11:00 a.m., Tuesday, April 23, 1974 Bayshore Inn, Vancouver, British Columbia.

DIRECTORS' REPORT TO THE SHAREHOLDERS

Commercial operations commenced on October 1, 1972 and 1973 was thus the Company's first full year of operation. Earnings for 1973 were $31,898,000 or $3.89 per share compared to the net loss of $1,215,000 incurred in the three month operating period in 1972. Earnings per share are based on the weighted average number of shares outstanding during the year. Costs, ore grades, metallurgical results and operating performance were consistent with objectives and substantial progress was made in repayment of the major loan financing undertaken to finance the development and construction of the Company's copper-molybdenum property in the Highland Valley of British Columbia.

The sections of this report that follow comprise a more comprehensive report on the 1973 operations and the general affairs of the Company.

Financial

Revenue from mine production, comprising copper, molybdenum and minor precious metals values, totalled $96,016,000 as compared to $10,636,000 in the three month operating period in 1972. Copper prices, which were at unduly low levels in 1972, began to increase in the early part of 1973 and were at a high level for the remainder of the year. Provision was made for Provincial mining taxes in the amount of $5,192,000 in 1973. The Company's earnings were exempt from Federal income taxes until December 31, 1973; provision for such taxes will be made in 1974 on a deferred and/or current basis as applicable.

The composition of the Company's long term debt and the changes therein in 1973 are set out in detail in Note 4 to the Financial Statements. During the year principal repayments and interest payments totalling $26,658,000 and $8,487,000 respectively were made. Interest not currently payable on Income Debentures was accrued and charged to earnings in the amount of $4,573,000. In January and February 1974 additional bank loan repayments of $3,600,000 and $5,706,000 respectively were made, which reduced the principal amount of the original $60,000,000 loans to $24,289,000.

Operations

In 1973 a total of 24.1 million tons of waste and 14.0 million tons of ore were mined, representing an average of almost 140,000 tons of material handled per mining day at a waste to ore ratio of 1.72:1.

The average daily milling rate of 35,459 tons for the first quarter was lower than the designed average daily milling rate of 38,000 tons. This rate was exceeded for the remaining nine months and the average for the year was slightly in excess of the design rate.

The milling, metallurgical and production data for the year were:

Tons of ore milled	13,987,154
Average tons milled per day	38,320
Average millhead grade	
– copper	.422%
– molybdenum	.017%
Average mill recovery	
– copper	89.5%
– molybdenum	71.9%
Pounds of payable metal in concentrate produced	(thousands)
– copper	102,180
– molybdenum	3,481
Ounces of silver produced (thousands)	431

Shipments totalling 86.4 million payable pounds of copper in concentrate and 3.4 million pounds of molybdenum in concentrate were made during the year. An additional shipment of 11.6 million payable pounds of copper in concentrate was made early in January 1974.

Net capital expenditures in 1973 were $3,290,000. In addition to normal capital replacements, the capital program included three projects undertaken to improve operating efficiencies and to meet additional needs for employee accommodation. These comprised the addition of a 15 cubic yard shovel, one 120 ton truck and one 200 ton truck to the mining operation, a major revision to the tailings system and an additional mobile home park at Logan Lake. The tailings system revision will reduce pumping costs and improve operating reliability. It includes re-routing part of the line through areas that were not available when the system was constructed originally. These projects were complete or virtually complete by year end.

The ore reserves delineated at the time the decision was made to bring the mine into production were 293 million tons of ore with an average grade of 0.427% copper and 0.014% molybdenum. A comprehensive program was undertaken in the last quarter of 1973 to define the total ore reserves contained in the Lornex property and to determine the optimum mining rate for extraction. As of this date the indication is that additional ore reserves contiguous to and beneath the presently planned open pit mine will be identified. It is expected that the program will be completed in 1974.

Employee Relations

At December 31, 1973 there were 653 employees of the Company of whom 474 were engaged in production and 179 were engaged in executive, technical, administrative or clerical functions.

The collective agreement between the Corporation and the United Steelworkers of America is in effect until June 30, 1974. There was a work stoppage for one and one-half days in July and an eight day work stoppage in October. Except for these occurrences employee relations have been reasonably good.

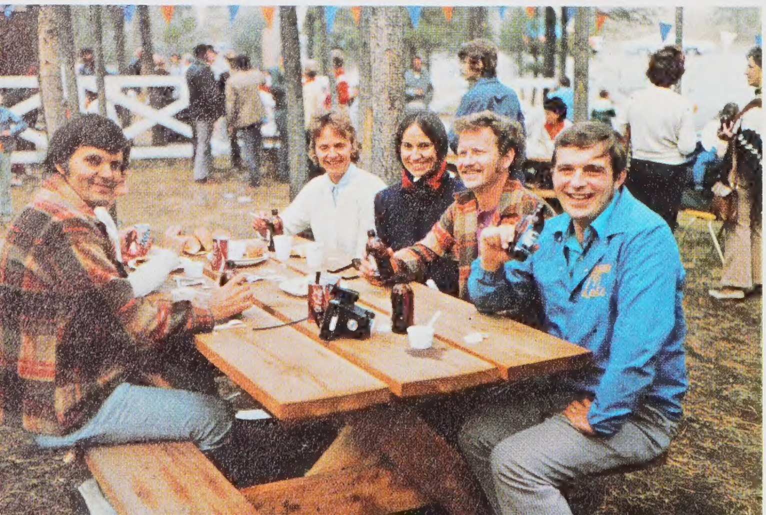
General Considerations

The Company's earnings are highly sensitive to the world price of copper and there is no reliable

LORNEX'S FIRST PICNIC, held well before the first snow, turned out to be a resounding success.

With just about everyone at the mine turning out, plus their families and friends, more than 1,000 took part in the day's activities. The weatherman cooperated completely and there were hot dogs, drinks and plenty of action for everybody.

The picnic was held at a nearby ranch so the program included such horsey events as a barrel race and musical chairs (saddles to be precise). There was also a tug of war, won by a strong-arm open pit crew, mucking and horse shoe pitching.



NEW EQUIPMENT AT LORNEX: GIANT-SIZE OF COURSE

Lornex added another mammoth electric shovel and a 200-ton-capacity dump truck to its array of heavy equipment. The truck is one of the few of that size in the world Fully loaded it weighs more than 350 tons and is powered by a locomotive diesel engine.

Lornex has 22 other haulage trucks carrying ore from the open pit to the crusher. They have a capacity of 120 tons each. The new shovel's capacity is 15 cubic yards (about 15 tons), the same as that of the four other shovels at the mine.

means of forecasting the price of this metal in 1974 and subsequent years. Lornex's entire copper production is sold to a group of Japanese smelting companies under a long term contract. The energy problem that confronted the Japanese late last year appears to be improving.

The Company's tax exempt period having expired, a charge against earnings will be required for Federal income taxes in 1974. Federal tax legislation is unclear and its effect on Lornex and other natural resource developers is uncertain. The Government of the Province of British Columbia has introduced Bill 31, a Mineral Royalties Act. If enacted in its present form it will have the direct and immediate effect on Lornex of reducing earnings in 1974 and future years by material amounts and will also reduce significantly the rate of repayment of the Company's debt.

Lornex has now established itself as an efficient world scale producer and further operating improvements are planned for 1974. The preliminary indications from the Company's ore delineation program are that its ore reserves will be increased. The effect of these positive factors can, as indicated, be modified or offset by forces beyond the Company's control but under reasonable and normal conditions Lornex can be expected to continue as a strong and viable enterprise.

Appreciation:

The year 1973 was successful in terms of operating results and in establishing a balanced operating position from which additional improvements will evolve. The Directors wish to extend their appreciation to the members of the Lornex organization whose efforts have made this possible.

Vancouver, B.C.,
February 27, 1974.

R. D. Armstrong,
President.

Auditors' Report

To the Shareholders of
Lornex Mining Corporation Ltd.:

We have examined the statement of financial position of Lornex Mining Corporation Ltd. as at December 31, 1973, and the statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these financial statements present fairly the financial position of the Company as at December 31, 1973 and the results of its operations and the changes in its financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Vancouver, British Columbia
February 6, 1974

COOPERS & LYBRAND
Chartered Accountants.

ACCOUNTING POLICIES

The principal accounting policies followed by Lornex Mining Corporation Ltd. are summarized hereunder:

REVENUE FROM MINE PRODUCTION AND VALUATION OF CONCENTRATES AWAITING SHIPMENT

A group of Japanese smelting companies has contracted to purchase the Company's entire production of copper concentrate for a period of twelve years expiring in 1984. A United States company has contracted to purchase the projected annual molybdenum concentrate production for a period of five years expiring in 1977.

Production is valued and taken into income as revenue from mine production at estimated realizable metal prices less provision for possible fluctuation in price; concentrates awaiting shipment are also valued on this basis. Adjustments are made to revenue from mine production with respect to concentrate shipments when the actual metal price is known and the final weight and assay adjustments are determined. Estimated smelting, refining and marketing charges are accrued at time of production and these charges are also adjusted with respect to shipments when the final weight and assay adjustments and marketing charges are determined.

At December 31, 1973 inventories of 20,248,370 payable lbs. of copper and 749,356 payable lbs. of molybdenum contained in concentrates awaiting shipment were valued as described above; the final price has been established in respect of a January 1974 shipment of approximately 11.6 million payable pounds of copper for which final weight and assay adjustments and marketing charges had not been determined.

CONVERSION OF UNITED STATES CURRENCY

The accounts in United States currency are stated in Canadian dollars on the following basis:

Current assets and current liabilities at year-end exchange rates; all other assets

and long term liabilities at rates in effect at time of transactions, and revenues and expenses at actual rates prevailing during the year.

MINE SUPPLIES

Mine supplies are valued at average cost.

DEPRECIATION AND AMORTIZATION

Depreciation is provided on mining equipment on a straight-line basis over the shorter of its physical life or the estimated life of the mine. The cost of plant and equipment, mining properties and preproduction expenditures is amortized on a unit-of-production basis over the estimated life of the mine.

INCOME AND MINING TAXES

Under applicable Canadian income tax legislation, the income of the Company was exempt until December 31, 1973.

A recent decision of the Federal Court of Appeal (presently under appeal in the Supreme Court of Canada) raises the possibility that a material portion of the income reported by the Company as being exempt under the provisions of the Income Tax Act may be subjected to tax. There is no satisfactory precedent upon which to base an estimate of any additional income taxes, in the event the Supreme Court establishes a different method of calculation of the tax exempt income.

Full provision has been made for Provincial mining taxes.

Deferred tax accounting procedures are being followed with respect to Provincial mining taxes and will be followed with respect to income taxes commencing in 1974.

Statement of Financial Position

DECEMBER 31, 1973

($000's omitted)

	1973	1972
CURRENT ASSETS:		
Cash and short term deposits	$ 5,883	$ 5,253
Accounts and settlements receivable and prepaid expenses	4,126	2,816
Concentrates awaiting shipment	18,773	2,844
Mine supplies	5,507	4,337
Total	34,289	15,250
Less:		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	5,591	3,751
Payable to Rio Algom Mines Limited	573	3,245
Provincial mining taxes payable	2,477	–
Long term debt due within one year (note 4)	4,523	6,153
Total	13,164	13,149
WORKING CAPITAL	21,125	2,101
Plant and equipment, less depreciation (note 2)	91,309	93,962
Mining properties and preproduction expenditures less amortization (note 3)	44,502	46,925
TOTAL ASSETS LESS CURRENT LIABILITIES	156,936	142,988
Deduct:		
Long term debt (note 4)	112,373	133,147
Deferred Provincial mining taxes	2,715	–
	115,088	133,147
EXCESS OF ASSETS OVER LIABILITIES	$ 41,848	$ 9,841
OWNERSHIP EVIDENCED BY:		
Capital stock (note 5)		
Authorized –		
9,500,000 common shares, par value of $1.00 each		
4,500,000 Class A shares, par value of $1.00 each		
Issued –		
8,214,662 common shares (7,331,904 shares in 1972)	$ 8,215	$ 7,332
– Class A shares (867,758 shares in 1972)	–	868
	8,215	8,200
Premium less discount on shares issued for cash (includes $94 premium on shares issued under stock option plan in 1973 and $6 in 1972).	2,950	2,856
Retained earnings (deficit)	30,683	(1,215)
Total	$ 41,848	$ 9,841

Approved on behalf of the Board:

NEIL B. IVORY, Director. R. D. ARMSTRONG, Director.

Statement of Earnings

YEAR ENDED DECEMBER 31, 1973

($000's omitted)

REVENUE:	1973	1972
Revenue from mine production	$ 96,016	$ 10,636
Less smelting, refining and marketing charges	14,187	1,689
Net revenue	81,829	8,947
Investment and other income	831	–
	82,660	8,947
EXPENSES:		
Operating costs	21,104	4,752
Administrative and general expenses	4,763	880
Amortization and depreciation	8,366	1,781
	34,233	7,413
Operating profit	48,427	1,534
Interest on long term debt	11,337	2,749
Earnings before Provincial mining taxes	37,090	(1,215)
Provincial mining taxes		
– Current	2,477	–
– Deferred	2,715	–
	5,192	–
NET EARNINGS (LOSS) FOR THE YEAR	$ 31,898	$ (1,215)
NET EARNINGS (LOSS) PER SHARE	$3.89	$(.15)

The statement of earnings for 1972 reflects only the three months from commencement of operations on October 1 to December 31, 1972.

Statement of Retained Earnings

YEAR ENDED DECEMBER 31, 1973

($000's omitted)

	1973	1972
BALANCE, beginning of year	$ (1,215)	$ –
Net earnings (loss) for the year	31,898	(1,215)
BALANCE, end of year	$ 30,683	$ (1,215)

Statement of Changes in Financial Position

YEAR ENDED DECEMBER 31, 1973

($000's omitted)

	1973	1972
SOURCE OF FUNDS:		
Operations		
Net earnings (loss) for year	$ 31,898	$ (1,215)
Add charges against earnings not involving current outlay of funds:		
Amortization and depreciation	8,366	1,781
Interest on Income Debentures, etc.	4,573	1,111
Deferred Provincial mining taxes	2,715	—
Total funds from operations	47,552	1,677
Bank loans	—	24,000
Units of 8½% Series A Income Debentures and shares	—	4,352
Housing loans (net)	—	407
Issue of common shares under stock option plan	109	7
	47,661	30,443
DISPOSITION OF FUNDS:		
Reduction of long term debt:		
Bank loans (see note)	24,775	5,900
8¾% Notes	253	253
	25,028	6,153
Expenditures on plant and equipment (net)	3,290	—
Expenditures on exploration, development and construction	—	27,041
Repayment of housing loans (net)	319	—
	28,637	33,194
Less charges not involving current outlay of funds:		
Value ascribed to share capital	—	348
Interest accrued prior to October 1, 1972 on Income Debentures and loans from associated companies	—	2,872
	—	3,220
	28,637	29,974
INCREASE IN WORKING CAPITAL	19,024	469
WORKING CAPITAL, beginning of year	2,101	1,632
WORKING CAPITAL, end of year	$ 21,125	$ 2,101

Note: Bank loan repayments in cash	$ 26,405
Less decrease in current portion of bank loans payable	1,630
Reduction in bank loans as above	$ 24,775

Notes to the Financial Statements

DECEMBER 31, 1973

1. ACCOUNTING POLICIES

The information on pages 8 and 9 presents a summary of certain accounting policies and is an integral part of these financial statements.

2. PLANT AND EQUIPMENT

	1973	1972
Plant and equipment at cost	**$101,648,308**	$ 98,419,798
Less accumulated depreciation	**10,339,517**	4,458,146
	$ 91,308,791	$ 93,961,652

3. MINING PROPERTIES AND PREPRODUCTION EXPENDITURES

	1973	1972
Mining properties, at cost	**$ 1,055,009**	$ 1,055,009
Less accumulated amortization	**62,622**	10,871
	992,387	1,044,138
Preproduction expenditures at cost	**46,266,282**	46,360,455
Less accumulated amortization	**2,756,377**	479,230
	43,509,905	45,881,225
	$ 44,502,292	$ 46,925,363

4. LONG TERM DEBT

	1973	1972
Bank loans (with interest and terms as stated hereunder)	**$ 33,595,000**	$ 60,000,000
Less portion included in current liabilities	**4,270,000**	5,900,000
Long term portion (including Can. $5,375,000 payable in U.S. dollars)	**29,325,000**	54,100,000
8¾% Notes due as stated hereunder	**26,583,233**	26,836,406
Less portion included in current liabilities ($250,000 U.S.)	**253,173**	253,173
Long term portion (1973 — $26,000,000 U.S.; 1972 — $26,250,000 U.S.)	**26,330,060**	26,583,233
8½% Series A Income Debentures due December 31, 1985	**44,093,000**	44,093,000
Housing loans	**358,648**	677,737
Accrued interest on Income Debentures	**12,265,958**	7,693,055
	$112,372,666	$133,147,025

Repayment of the bank loans is collaterally secured under a Trust Deed by the pledge of first mortgage bonds, secured by a first fixed and specific charge and a first floating charge on the assets of the Company. The interest rate on such loans is 1¼% above the minimum commercial

lending rate adjustable from time to time by each bank independently; the December 31, 1973 rate was 10¾% per annum.

Repayment of the 8¾% Notes is collaterally secured under a Trust Deed by the pledge of second mortgage bonds, secured by a second fixed and specific charge and a second floating charge on the assets of the Company.

Under the terms of the Bank Loan Agreement and the Japanese Financing Agreement 90% of the Company's net operating profit as defined is to be applied to repayment of the bank loans until repaid in full and thereafter to repayment of the 8¾% Notes. The cumulative minimum repayments of principal required to be made are as follows:

	Cumulative Minimum Repayments of Principal	
Due In	Bank Loans	8¾% Notes
1974	$ 16,300,000	500,000 U.S.
1975	29,300,000	750,000 U.S.
1976	42,300,000	1,000,000 U.S.
1977	54,400,000	1,250,000 U.S.
1978	60,000,000	8,350,000 U.S.
1979	—	21,650,000 U.S.
1980	—	26,500,000 U.S.

To December 31, 1973 repayments totalling $23,904,000 and $250,000 U.S. have been made on the bank loans and 8¾% Notes respectively, thereby reducing the cumulative minimum repayments shown above by these amounts; the cumulative bank loan repayments of $16,300,000 due in 1974 have thus been more than satisfied. In addition a further prepayment of $2,501,000 was made against the bank loans bringing the total bank loan repayments during 1973 to $26,405,000.

The principal amount of the Income Debentures is to be repaid by way of annual sinking fund payments from all of the operating profits of the Company after all other forms of long term debt have been paid in full. The amounts and timing of the required sinking fund payments are defined in the Income Debenture Indenture and are dependent on the operating profits of the Company together with certain other factors. The sinking fund payments are to be used to redeem the Income Debentures at par. Of the Income Debentures of $44,093,000 outstanding at December 31, 1973 $36,097,000 principal amount is owned by the parent company, Rio Algom Mines Limited.

The accrued interest of $12,265,958 on Income Debentures at December 31, 1973 may not be paid until the required interest and principal repayments have been made and certain other conditions have been met under the terms of the Bank Loan Agreement and the Japanese Financing Agreement.

5. CAPITAL STOCK

	Common		Class A	
Shares Issued:	Shares	Amount Paid Up	Shares	Amount Paid Up
At December 31, 1972	7,331,904	$7,331,904	867,758	$ 867,758
Under stock option plan	15,000	15,000	—	—
Conversion of Class A to common shares	867,758	867,758	(867,758)	(867,758)
Balance, December 31, 1973	8,214,662	$8,214,662	—	$ —

The Class A shares are non-voting, are not entitled to dividends, and are convertible to common shares at any time at the option of the holder on the basis of one common share for each Class A share.

At December 31, 1973, 844,660 common shares were reserved:

(a) 760,560 common shares for issue in exchange for the 760,560 Class A shares which may be issued under the terms of the Construction and Management Agreement;

(b) 84,100 common shares for issue under a Stock Option Plan. Options may be granted to employees of the Company and to certain employees of Rio Algom Mines Limited. Outstanding options have been granted to purchase 64,600 common shares at prices varying from $7.29 to $8.65 per share; these options expire on varying dates from September 27, 1976 to April 16, 1979.

In addition 760,560 Class A shares are reserved to satisfy obligations of the Company which may arise under the provisions of the Construction and Management Agreement with Rio Algom (note 6(a)).

The Trust Deeds and Indentures prohibit the payment of dividends until all loans and accrued interest have been paid in full.

6. COMMITMENTS AND CONTINGENT LIABILITIES

(a) Rio Algom Mines Limited has agreed to supervise and manage the business of the Company until December 1, 1984 and to incur and pay, on behalf of the Company, operating costs of the Company incurred prior to August 1, 1976. The Company has agreed to pay Rio Algom a management fee of $250,000 per annum.

If the Company is unable to reimburse Rio Algom for any of the aforementioned costs Rio Algom may elect to receive Units of the Company's Income Debentures and Class A shares instead of cash at a later date. The maximum number of such Units which could be issued is 9,507, comprised of $9,507,000 principal amount of Income Debentures and 760,560 Class A shares.

(b) The Company has a contingent liability to buy back 231 houses and 42 mobile home lots at the Logan Lake townsite for $5,577,517 until December 31, 1982.

7. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

During the year ended December 31, 1973 the aggregate direct remuneration paid or payable by the Company to the directors and senior officers of the Company was $176,415.

Rio Algom

Rio Tinto

Printed in Canada.